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CROSSCURRENTS IN THE MONEY MARKET

THE money market, as a harassed observer remarked the other day, probably can be summed up best in the famous words of Shakespeare: ". . . full of sound and fury, signifying nothing." While this may be something of an overstatement, it is nonetheless true that lenders today, in trying to appraise the supply-demand outlook, confront an extraordinary number of uncertainties and crosscurrents.

The resulting confusion has been apparent in recent months in the marketplace. To illustrate, long-term Government bonds, after breaking to new lows at the end of December, turned around and climbed 3-4 points in January, one of the sharpest rises in history. Last month, however, they promptly gave up one-third of the gain. Similarly, at the end of January, for the first time in well over a year, one dealer in bankers acceptances whittled rates by one-eighth percent; barely a week later, he reversed his action. Finally, after a precipitous drop from more than 3.30 percent at the year-end to less than 3 percent in mid-February, the Dow-Jones index of municipal bond yields has climbed back to 3.12 percent.

Despite these ups and downs, money rates plainly have eased since December. Early this month, for example, Garvin, Bantel and Co., leading money brokers, announced a one-eighth percentage point reduction in the time-money rate - the interest charged by banks on short-term loans secured by stock exchange collateral. In explaining the move, a spokesman for the firm said: "There is a little more money around." Banks, chiefly those outside New York, "have better liquidity," he added. Similarly, corporate borrowers lately have been getting a better price - perhaps 15-20 basis points better - on their offerings. In the field of home finance, the same trend has been faintly visible. At the end of February the Federal National Mortgage Association sold an 11-month issue of Secondary Market Operations debentures at 4 percent; six weeks earlier Fannie Mae had to pay 4-1/8 percent for 8-month funds.

This adjustment in fixed income obligations - and its counterpart in stocks - apparently reflects the growing belief, in both Government and financial circles, that the boom lately has lost some of its exuberance. As to Washington, a recent statement by William McChesney Martin, chairman of the Federal Reserve Board, is revealing. "We are trying to determine whether the wind has shifted - whether

it is still blowing inflation or perhaps less strongly so," he said the other day. At the same time, he indicated that the monetary policy of the FRB has changed from aggressive to passive restraint.

Still more significant in this regard is the slackening in demand for bank credit. In the first two months of 1957, in banks in 93 cities outside New York, commercial, industrial, and farm loans declined by $675 million from their year-end peak. This figure compares with a drop of only $385 million in the corresponding months of 1956. By the same token, total loans of these institutions since January 1 are down nearly $1 billion, against a drop of only $400-odd million in the like 1956 period. Some rise in borrowings - primarily for tax purposes - is likely to occur in March. However, leading bankers now are figuring on a seasonal increase no more than two-thirds of what it was a year ago.

So much for the current status of interest rates. As for the outlook, it's worth noting that an increasing number of authorities, while differing on timing, expect the turn toward easier credit to grow more pronounced this year. For example, in a memorandum to portfolio managers, a leading Wall Street bond firm puts the supply of new long-term funds at $22.1 billion in 1957, just $1.1 billion, or 4.7 percent less than the demand, a gap somewhat smaller than that in recent years. Hence, the firm suggests, borrowers may have less difficulty in filling their capital needs this year than was the case in 1955-56. In fact, "it is possible that at times available funds may equal or temporarily exceed demand."

Similarly, John F. Austin, president of the Mortgage Bankers Association of America, looks for some easing of credit at the end of the first quarter. Again, a newly organized firm of mortgage brokers, which has been trying, without marked success, to interest pension funds in home loans, is highly optimistic about its short-term prospects. One FHA mortgagee is even more bullish. It actually has gone on record suggesting that a shortage of desirable VA and FHA home loans may develop this year.

A hard look at the current and prospective state of business furnishes considerable support for such views. On the other hand, two forces now at work in the money market - a shift in U. S. thrift habits and the precarious state of the Treasury's finances - are tugging, for the moment at any rate, in the opposite direction. Let's examine each in turn.

As to savings, the Federal Reserve Board, in granting commercial banks the right to pay as much as 3 percent on time deposits last December, set off a chain reaction throughout the entire realm of thrift. For those commercial banks which have raised their rates - the Chase-Manhattan in New York City being one conspicuous example - have built up their savings totals rapidly, frequently at the expense of other thrift institutions.

A few figures illustrate the point. In January, according to the FRB, time deposits in the Nation's commercial banks rose by an unprecedented $1 billion,

compared to only $200 million in January of 1956. In contrast, regular deposits in the Nation's 527 mutual savings banks increased only $63 million in January, less than half of the gain of $140 million scored 12 months previous. By the same token, the Federal Home Loan Bank Board reported that the January net savings inflow for U. S. savings and loan associations totaled $282 million, one-third less than that of January 1956 and the lowest figure for the month since the post-Korean wave of scare buying in 1951. Complete figures for February are not yet available. However, based on fragmentary reports from a number of thrift institutions, it is evident that the sharp year-to-year decline has continued.

This shift has an ominous implication for the supply of mortgage money. As Thurman Lee, head of the Dry Dock Savings Bank of New York, pointed out, commercial banks do not necessarily invest time deposits in mortgages or other long-term instruments. Hence, in Mr. Lee's opinion, 'a savings dollar with them is a dollar lost to the capital market.' As a result, he added, the ability of his bank to purchase home loans 'has been crippled, temporarily at least.'

Nor, apparently, is Dry Dock the only savings institution in this plight. Savings and loan associations, according to FHLBB, extended $690 million in mortgage loans in January, 3 percent less than in January 1956. Similarly, mortgage holdings of all mutual savings banks in January rose by only $136 million, against $192 million in 1956. The increase was the smallest monthly gain in nearly three years.

More disturbing, not merely to mortgage lenders, but to the entire money market, are the increasingly serious financial straits in which the U. S. Treasury, biggest borrower of all, now finds itself. True, the budget for the current fiscal year is expected to produce a surplus on current account. However, in recent months, owners of savings bonds, dissatisfied with their low return, have been cashing in their holdings apace. Hence the Treasury has been faced with a sudden and unlooked-for drain on its resources. In February, for example, redemptions of savings bonds of all series exceeded sales by more than $250 million, a jump of nearly tenfold over the like year-ago month. Since July 1, the start of the new fiscal year, the savings bond program has drained $1.5 billion from the public purse.

As a consequence, since last fall the Treasury has been borrowing more heavily. It tried to raise funds, first, through special offerings of short-term bills. This year, moreover, it gradually has been increasing the amount of its regular weekly bill offering. Such expedients, however, have proved inadequate to the need. Hence last week (March 4), in a move unprecedented for peacetime, the Treasury announced that it planned to raise $2-$3 billion of new money later this month. Owing to the heavy tax payments which accrue, March is traditionally one month in which the Treasury does not borrow. In fact, in recent years this has been the season in which it has retired part of its outstanding debt.

Thus, announcement of the new issue has tended to cast a pall over the financial community. This is particularly true in view of the lukewarm reception given

the Treasury's last piece of financing, a refunding in mid-February. At that time, out of a total of nearly $10 billion of maturing notes and certificates, nearly $900 million were not exchanged for new securities but were turned in for cash. Indeed, some 17 percent of the total holdings outside the Federal Reserve Banks had to be paid off.

How long this state of affairs will continue is by no means clear. Legislation designed to sweeten the yields on savings bonds (retroactive to February 1, by the way) is making its way through Congress. When it takes effect, it presumably will go far toward plugging the drain. However, for the short-term at least, the Treasury will remain a source of uncertainty, not to say concern, to investors generally.

These are the crosscurrents mentioned earlier. While they tend to obscure the trend - and make life difficult for money market observers - in the end their effect is apt to prove merely transitory. For unless a good many signs and portents are misleading, the main current, i. e. the slackening of prosperity, is running toward easier credit..

In this connection the Harris Trust and Savings Bank of Chicago recently pointed out that after nearly $2\frac{1}{2}$ years of a steady upswing in business, widespread weaknesses are beginning to appear. In particular, it underscored the fact that eight leading indicators, selected by the National Bureau of Economic Research (including new orders for durable goods, commodity prices, average hours worked per week, and business failures), have been declining for more than six months. Based on past experience, such a decline points to an impending drop in business activity generally.

Other storm signals are flying. Some leading industrial concerns recently have announced cutbacks in expenditures for plant and equipment. The price of steel scrap, a virtually infallible barometer of future activity in the industry, has been sliding for weeks, and steel operations now have begun to follow suit. Production of paperboard, another key material, also has fallen off steadily. It now seems likely, in short, that another inventory recession - or, as some prefer to call it, a rolling readjustment - has begun. In the circumstances, sooner or later, money inevitably will grow easier.